No. 12,960

IN THE

United States Court of Appeals

For the Ninth Circuit

HARDWARE MUTUAL INSURANCE CO. OF MINNESOTA, a corporation,
Appellant,

vs.

MILDRED A. DUNWOODY, HAROLD A. GOLDMAN, MYRTLE GOLDMAN, HAROLD F. BARUH, and DORIS G. BARUH,
Appellees.

BRIEF OF APPELLEES, HAROLD A. GOLDMAN, MYRTLE GOLDMAN, HAROLD F. BARUH AND DORIS G. BARUH.

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JURISDICTION.

Appellant alleged (R. 3-4) and appellees Harold A. Goldman, Myrtle Goldman, Harold F. Baruh and Doris G. Baruh (hereinafter collectively referred to as lessee appellees) and appellee Dunwoody (hereinafter referred to as Dunwoody) admitted (R. 8, 27) that the parties hereto are citizens of different states and that the amount in controversy is in excess of

$3,000.00, exclusive of interest and costs. It is upon this basis that the District Court of the United States for the Northern District of California, Southern Division, had jurisdiction to hear this case under the Federal Declaratory Judgment Act (28 U.S.C. Section 2201).

This Court has jurisdiction to review the decision of said Court under 28 U.S.C. Sections 1291 and 1294.

STATEMENT OF THE CASE.

Practically all of the facts in this case were presented to the District Court by stipulation of the parties hereto (R. 37-66). In its statement of the case appellant has attempted to present a concise statement of these facts. In so doing appellant has omitted therefrom certain facts which are essential to the determination of the issue involved. These facts are as follows:

(1) The only subrogation clause contained in the policy of fire insurance issued by the appellant to Dunwoody, which was the California Standard Form Fire Insurance Policy then in effect, reads as follows:

> "SUBROGATION. If this company shall claim that the fire was caused by the act or neglect of any person or corporation, this company shall, on payment of the loss be subrogated to the extent of such payment to all right of recovery by the insured for the loss resulting therefrom, and such right shall be assigned to this company by the

insured on receiving such payment." (R. 38, 47, lines 144-146).

(2) The fire which, on April 8, 1949, totally destroyed the buildings covered by said policy was due to causes unknown (R. 41).

(3) At the time of said destruction of said buildings, the lessee appellees were, and they still are, successor lessees of the premises upon which said buildings were located under a lease wherein Dunwoody is the lessor (R. 39). Paragraph 12 of said lease reads in part as follows:

> "12. Should the whole or any part of any building or buildings at any time standing on the demised premises be partially or totally destroyed by fire after the commencement of the term hereof, the same shall be restored by the Tenant at its own expense without unnecessary delay.
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> * * * * * * *
>
> "Notwithstanding anything else herein contained to the contrary, if the premises or a portion thereof be damaged by fire, upon the payment of the insurance by the insurance company of the loss to the parties hereto as their interests may appear, all of such payment may be used by the Landlord for the purpose of restoring the portion damaged if the Landlord desires" (R. 40-41).

(4) At the time of said fire there was in full force and effect a policy of fire insurance issued by the Security Insurance Company of New Haven, in the amount of $36,795.00, covering the same premises

covered by the policy of fire insurance issued by appellant to Dunwoody. The insured named in said policy were appellees Harold F. Baruh and Harold A. Goldman and/or Dunwoody. Loss under said policy was to be adjusted with and payable to said appellees Harold F. Baruh and Harold A. Goldman (R. 41-42). After said fire said Security Insurance Company admitted liability in full under said policy of insurance and paid thereunder to appellees Harold F. Baruh and Harold A. Goldman the sum of $25,000.00, and retained, as provided by the depreciation endorsement clause contained in said policy, the sum of $11,743.89 to be paid to said parties when said buildings are rebuilt; that of the $25,000.00 paid to the appellees Harold F. Baruh and Harold A. Goldman they expended the sum of $1173.89 to remove the debris upon the property caused by the burned buildings and the balance, at the request of Dunwoody, was placed by said appellees Harold F. Baruh and Harold A. Goldman in a savings account in a bank in San Francisco, to be withdrawn only upon the signatures of Dunwoody and appellee Harold F. Baruh or appellee Harold A. Goldman (R. 65-66).

Appellant in its complaint prayed as follows:

"(1) That the Court adjudge that the plaintiff is not liable to defendant Mildred A. Dunwoody in any amount whatsoever;

(2) That should the Court decree that plaintiff is liable to defendant Mildred A. Dunwoody, the Court will determine the amount of said liability

and enter judgment against defendants Harold A. Goldman, Myrtle Goldman, Harold F. Baruh and Doris G. Baruh for said amount.

(3) * * * * * * *

(4) * * * * * * *"

(R. 7).

The Court found in favor of all of the appellees and adjudged that Dunwoody is entitled to recover from appellant the sum of $10,000.00 and that upon payment of said sum to Dunwoody appellant is not entitled to be subrogated to any of the rights of Dunwoody against lessee appellees (R. 82-83).

Appellant now concedes (Br. 7) that insofar as said judgment requires the payment by appellant of said sum of $10,000.00 to Dunwoody and holds that upon said payment appellant is not entitled to judgment for said amount against the lessee appellees, said judgment is correct. Appellant now contends (Br. 7) that the Court "should have included in the judgment a declaration that upon full restoration of the buildings appellant would be entitled to a return of the amount so paid, and that in the event of a failure upon the part of lessees to fulfill their obligation to restore the buildings appellant would be entitled to be subrogated to appellee Dunwoody's right to enforce this obligation—such subrogation to be *pro tanto* to the extent of the amount paid by appellant and subject to the prior right of appellee Dunwoody to have full indemnification for her loss" (Br. 7-8).

In this brief we will confine ourselves to answering this contention so far as it concerns the lessee appellees.

QUESTION PRESENTED.

Upon payment of the sum of $10,000.00 by appellant to Dunwoody under the policy of fire insurance issued by it to her, is appellant entitled to be subrogated to the right of Dunwoody under the aforesaid lease to have the lessee appellees rebuild the buildings destroyed by fire?

SUMMARY OF ARGUMENT.

Since appellant is no longer seeking a monetary judgment against lessee appellees as prayed for in its complaint, but now is only seeking to be subrogated to the right of Dunwoody to have the lessee appellees rebuild the buildings destroyed by fire, and since the lessee appellees do not question their obligation to rebuild said buildings, it might appear, at first blush, that the case has lost all importance to the lessee appellees. However, the only person to whom lessee appellees are so obligated is Dunwoody and the lessee appellees insist that no additional person be given the right to interfere in the performance, or non-performance, or any negotiations in relation to, or any adjustment of, said obligation. That the lessee appellees have the right to so insist will be evident from our argument wherein we will show the following:

1. That this Court and the Supreme Court of the State of California have each recognized and applied the doctrine that, upon payment of the loss under a policy, an insurer does not become subrogated to the rights of the insured under a contract with a third party unless the loss insured against is a debt for which such third party is primarily liable and the insurer is secondarily liable.

2. That in the instant case there is no debt for which the lessee appellees are primarily liable and the appellant is secondarily liable because the appellant insured the buildings destroyed by fire and not the obligation of lessee appellees under their lease with Dunwoody to rebuild said buildings.

3. That the subrogation clause in the policy issued by appellant to Dunwoody limited appellant's right of subrogation to cases where appellant claims that the fire was caused by the act or neglect of a third person, which is not the situation in the instant case where all parties have agreed that the fire which destroyed said buildings was due to causes unknown.

4. That since the trial Court rendered judgment in favor of appellees and against appellant, appellant has no right to claim in this Court relief not prayed for in its complaint.

ARGUMENT.

Admittedly, the policy of fire insurance issued by the appellant to Dunwoody does not contain any provision granting the appellant the right of subrogation to contract rights belonging to Dunwoody (Br. 16). Appellant's argument is based upon its contentions that (1) upon payment of the loss under a policy, an insurer in every instance becomes subrogated to the rights of the insured under contracts with third parties and (2) said right of subrogation arises by operation of law and is not dependent upon any express provision therefor in the policy (Br. 14-17).

It is our contention that (1) where, as in the instant case, there is no primary liability on the part of such third parties for the loss insured against, the insurer is not entitled to be subrogated to the rights of the insured under a contract with such third parties, and (2) the right of subrogation which arises by operation of law may be limited by a provision inserted in the policy such as the subrogation clause contained in the policy issued by appellant to Dunwoody.

I.

UPON PAYMENT OF THE LOSS UNDER A POLICY, AN INSURER DOES NOT BECOME SUBROGATED TO THE RIGHTS OF THE INSURED UNDER A CONTRACT WITH A THIRD PARTY UNLESS THE LOSS INSURED AGAINST IS A DEBT FOR WHICH SUCH THIRD PARTY IS PRIMARILY LIABLE AND THE INSURER IS SECONDARILY LIABLE.

The doctrine that an insurer is not entitled to be subrogated to the rights of the insured under a con-

tract with a third party unless the loss insured against is a debt for which such third party is primarily liable and the insurer is secondarily liable has been recognized and applied in the following two cases wherein the Courts denied the insurer the right to be subrogated to the contract rights of the insured under a lease with a third party.

In *Plate Glass Underwriters' Mutual Insurance Co. v. Ridgewood Realty Co.* (1925), 219 Mo. App. 186, 269 S.W. 659, plaintiff insurance company insured a tenant against breakage of plate glass. Plaintiff replaced some plate glass which had been blown out by a windstorm. Subsequently it discovered that the insured was a tenant under a lease which required the lessor to repair the damage done. Plaintiff sought to recover from the landlord the amount it had expended in replacing the glass on the theory that it had only agreed to indemnify the tenant against the loss of damage in question; that by the terms of the lease such loss was primarily the loss of the landlord and should have been borne by it; and that it was subrogated to the rights of the insured under the subrogation clause in the policy which provided that the insurer upon payment of a loss was entitled to be subrogated to all rights of the assured against any person as respects such loss to the extent of its interest. In holding that the insurer by paying for the repairs did not become subrogated to the rights of the tenant against the landlord, the Court said at page 662:

> "But we do not think any rights of subrogation exist in this case. Subrogation is a child of equity,

which in later years has grown into and become a principle of law; but its origin or basis is in the nature of things, i.e., it grows out of natural justice demanded by the facts of the situation. For instance, if one secondarily liable for a debt pays it, he is entitled as against the debtor who is primarily liable to be subrogated to the creditor's rights, and such right of subrogation arises, by operation of law, out of that situation with or without any agreement to that effect. Loewenstein v. Queen Ins. Co., 227 Mo. 100, 127 S.W. 72. Now, the insurance company in the case at bar did not agree to insure or guarantee to the insured the payment of any debt, or the performance of any obligation on the part of insured's landlord. It merely agreed to insure the plate glass, i.e., the property itself, for a cash consideration, to wit, the premiums paid by insured. The insurance contract was one solely between the two parties thereto, and the insurance company only paid what it contracted primarily to do; but now, notwithstanding it still retains the premiums or the benefit of its contract, it seeks reimbursement from the landlord on the basis that the latter, under a wholly separate and independent contract should have done so. We see no basis of subrogation arising out of the circumstances herein, and are of the opinion that the subrogation clause in the insurance contract only applies to circumstances in which the law creates the right of subrogation. The plaintiff insured the property itself, not a debt due the tenant. Havens v. Germania Ins. Co., 135 Mo. 649, 658, 659, 37 S.W. 497. The mere fact that the tenant might thus have two sources to which he could look for repair or re-

imbursement does not give the plaintiff the right to be subrogated to that right as to one of such sources. Ely v. Ely, 80 Ill. 532; see also Washington etc. Co. v. Weymouth etc. Ins. Co., 135 Mass. 503; Foley v. Manufacturers, etc. Ins. Co., 152 N.Y. 131, 46 N.E. 318, 43 L.R.A. 664; Heller v. Royal Ins. Co., 177 Pa. 262, 35 A. 726, 34 L.R.A. 600; Fire Ass'n v. Patton, 15 N.M. 304, 107 P. 679, 27 L.R.A. (N.S.) 420; Milwaukee etc. Ins. Co. v. Ramsay, 76 Or. 570, 149 P. 542, L.R.A. 1916A, 556; Ann. Cas. 1917B, 1132.

"The English case of Darrell v. Tibbitts, 5 Q.B.D. 560, cited by appellant and hereinabove referred to, if in point, would seem to be contrary to the general weight of authority, and hence is not to be followed on the point in question." (Underscoring added.)

In *Alexandra Restaurant v. New Hampshire Ins. Co.* (1947), 71 N.Y.S. (2d) 515, plaintiff, lessee of a restaurant, was insured by defendant insurance company against loss by fire on improvements of a structural character. The subrogation clause in the policy provided that the insurer could require from the insured an assignment of all right of recovery against any party "to the extent that payment therefor is made by this Company". Without fault of plaintiff or its landlord, a fire occurred causing damage to the improvements. Plaintiff's landlord under the terms of the lease became obligated to repair the damage and did so prior to the time plaintiff's policy became payable. In holding that the plaintiff had suffered a loss and that the insurance company was not entitled

to be subrogated to the rights of the plaintiff against the landlord under the lease, the Court said at page 520:

> "Commenting on the English cases, Richards Law of Insurance, 4th Ed., Sec. 54, pp. 81-83, says: 'If an insurer after loss is a mere surety for some obligor primarily liable, this rule would seem to be indubitably sound, but other courts in this country do not seem disposed to press to such an extreme either the doctrine of indemnity or that of subrogation when applied to the law of insurance. They seem rather inclined to look upon a contract of insurance upon property, if valid and unobjectionable when made, as an absolute promise by the insurer, subject to all the terms of the policy, to pay the damage sustained by the property as measured by its cash or market value (of course, however, not exceeding the amount of insurance), and they declare that inasmuch as premiums are estimated upon that measure of liability any other basis of indemnity is inequitable in principle besides being inconvenient in practice.'
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> "* * * The parties agreed that the insurer would make good a 'direct loss and damage by fire' to 'property' to the extent of its 'actual cash value'. The loss occurred and established the rights of the parties. This was the contract between the insured and the insurer. It was not a contract of surety that the landlord would perform his contractual obligation which was wholly independent of any relation to the insurance company.
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> * * * * * * *

"Plaintiff concededly had an insurable interest when the policy was issued and at the time of the loss. The loss was not caused by any wrongful act of either the landlord or the insured. Defendant's policy insured the property and not the debt due the insured from its landlord. The policy did not contain a clause specifically granting the insurer subrogation to contract rights belonging to insured. In the light of these facts and all the facts stipulated to in this regard it is difficult to see why under the subrogation clause in question, the ultimate loss should fall upon the landlord while the insurance company though accepting and retaining its premium for the precise coverage of loss that occurred, should have no obligation or liability whatever. Cf. Richards, Law of Insurance (4th Ed.), Sec. 54, p. 80." (Underscoring added.)

The instant case is analogous to each of the foregoing two cases in the following respects:

(1) In the instant case, as in each of said cases, the insurer is seeking to be subrogated to the contract rights of the insured under a lease with third parties.

(2) In the instant case, as in each of said cases, the loss insured against was not caused by said third parties.

(3) In the instant case, the obligation of the third parties under a lease is to rebuild the buildings destroyed by fire. In the *Plate Glass* case, supra, the obligation of the third party under a lease was to

"rebuild said building or repair such damage." In the *Alexandra* case, supra, the obligation of the third party under a lease was to repair the damage.

(4) In the instant case, as in each of said cases, the insurer has not insured said contractual obligation of the third parties under a lease, but only the property referred to in the policy of insurance.

(5) In the instant case, as in each of said cases, said obligation of the third parties is independent of that of the insurer to pay the insured the amount it contracted to pay in the policy for the loss sustained.

(6) In the instant case, as in each of said cases, the insurer is primarily liable to the insured for the amount of the loss insured against and said third parties are primarily liable to the insured for the performance of said contractual obligation under said lease.

Since the loss insured against under the policy is not a debt for which the third parties are primarily liable and the insurer secondarily liable, appellant is not entitled to be subrogated to the right of Dunwoody against the lessee appellees under said lease.

A. The United States Circuit Court of Appeals for the Ninth Circuit and the Supreme Court of the State of California have each recognized and applied said doctrine.

The views of this Court on the question as to whether or not an insurer, upon payment of a loss under a policy, becomes subrogated to the rights of

the insured under a contract with a third person are expressed in *American Surety Co. v. Bank of California* (1943, C.C.A. 9), 133 Fed. (2d) 160. In that case, this Court said at page 162:

> "The right of subrogation is a creature of equity, applicable where one person is required to pay a debt for which another is primarily responsible, and which the latter should in equity discharge. In theory one person is substituted to the claim of another, but only when the equities as between the parties preponderate in favor of the plaintiff. That is, a surety's right of recovery from a third party through subrogation does not follow, as of course, upon proof that the losing but recompensed party could have recovered from the third party. Accordingly, subrogation will not operate against an innocent person wronged by a principal's fraud. A surety may pursue the independent right of action of the original creditor against a third person, but it must appear that said third person participated in the wrongful act involved or that he was negligent, for the right to recover from a third person is merely conditional in contrast to the right to recover from the principal which is absolute. The equities of the one asking for subrogation must be superior to those of his adversary. If the equities are equal or if the defendant has the greater equity, subrogation will not be applied to shift the loss.
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> "That the law of Oregon is in accord with the principles above set forth is indicated by American Central Ins. Co. v. Weller, 106 Or. 494,

212 P. 803. There, the State Supreme Court held that the insurer's payment of the amount due on a policy, protecting the assignee of a conditional sales contract against loss caused by conversion of an automobile, satisfied the debt in that amount as against defendant, the guarantor of the debt by the assignment of the sales contract to the assignee. The court determined that the rules as to subrogation had no application to the situation in question and narrowly limited that application. Admittedly, the facts vary widely from those in the instant case, but the court's limitation of the subrogation doctrine is significant.

"At first glance, Chicago, St. Louis etc. R. Co. v. Pullman etc. Co. 139 U.S. 79, 11 S. Ct. 490, 35 L. Ed. 97, cited by Insurers, seems contrary to the result reached in the case at bar. There, the insurance company paid the Pullman Company the amount due on a fire insurance policy covering a sleeping car, and subsequently was allowed to recover the said amount by subrogation to the rights of the Pullman Company against the railroad. The railroad was using the car under a contract with the Pullman Company, in which it agreed to pay any damage to the car occasioned by accident or casualty. It was found that under the contract the railroad was primarily liable for the fire damage to the car, whereas the liability of the insurance company was secondary. We agree with the Oregon Supreme Court when it stated in the Weller case that an insurer, having paid a loss, is not entitled to the right of subrogation by virtue of a contract between insured and a third party unless the

contract shows primary liability on the part of such third person for loss of the property insured. In the case at bar there was no express contract on the part of Bank in favor of Interior as there was on the part of the railroad in the Pullman case. Furthermore, there was no primary liability on the part of a third person, the bank, for the loss; the primary liability rested on the employee Crowe. Therefore, the Pullman case is not authority in favor of Insurers herein." (Underscoring added.)

The views of the Supreme Court of the State of California on this question of subrogation to contract rights of the insured are in accord with those of this Court. These views are expressed in *Meyer v. Bank of America etc. Assn.* (1938), 11 Cal. (2d) 92, wherein the Court said at page 102:

"Thus, it may be observed that there are two lines of cases governing the questions here presented, each wholly at variance with the other. We think the great weight of authority rests with the group last referred to, and that the principles there announced, in good conscience ought to be applied to the circumstances of this case. As stated hereinbefore, the right to maintain an action of this kind and to a recovery thereunder involves a consideration of, and must necessarily depend upon the respective equities of the parties. Here, the indemnitor has discharged its primary contract liability. It has paid what it contracted to pay, and has retained to its own use the premiums and benefits of such contract. It now seeks to recover from the bank the amount

thus paid. It must be conceded that the bank is an innocent third party, whose duty to the employer was based upon an entirely different theory of contract, with which the indemnitor was not in privity. Neither the indemnitor nor the bank was the wrongdoer, but by independent contract obligation each was liable to the employer. In equity, it cannot be said that the satisfaction by the bonding company of its primary liability should entitle it to recover against the bank upon a totally different liability. The bank, not being a wrongdoer, but in the ordinary course of banking business, paid money upon these checks, the genuineness of which it had no reason to doubt, and from which it received no benefits. The primary cause of the loss was the forgeries committed by the employee, whose integrity was at least impliedly vouched for by his employer to the bank. We cannot say that as between the bank and the paid indemnitor, the bank should stand the loss. Under the facts of this case, as is stated in Northern Trust Co. v. Consolidated Elevator Co., 142 Minn. 132 (171 N.W. 265, 4 A.L.R. 510): 'The right to recover from a *third person* does not stand on the same footing as the right to recover from the *principal*. (Italics added.)'

"Our conclusion, as hereinbefore has appeared, is that since the bonding company had no superior equities, it was not entitled to be subrogated to any claim plaintiff might have had against the bank." (Underscoring added.)

In light of the fact that the fire which destroyed the insured buildings was not caused by any of the

lessee appellees but was due to causes unknown (R. 41), it cannot be said that there is any superior equity in favor of appellant which would entitle it to be subrogated to the rights of Dunwoody under her lease with lessee appellees.

B. The American cases which have applied the English rule that an insurer, upon payment of a loss, becomes subrogated to all contract rights of the insured are distinguishable from the instant case.

We concede that under the English rule set forth in *Darrell v. Tibbitts* (1878), 5 Q.B.D. 560 (Br. 13), an insurer, upon payment of a loss, is entitled in every instance to be subrogated to all rights of the insured under contracts with third persons respecting the subject matter insured. We recognize that there are American cases, including those cited by appellant (Br. 8-14), which purport to follow the English rule to the point at least of holding that, upon payment of a loss under a policy, an insurer becomes subrogated to the rights of the insured under a contract with a third person when the loss insured against is a debt for which such third person is primarily liable and the insurer is secondarily liable. These cases are distinguishable from the instant case in that in every one of said cases the third party was responsible and agreed to pay for the loss insured against, whereas in the instant case the lessee appellees were not responsible and did not agree to pay for the loss insured against, but merely to rebuild the buildings destroyed by fire. There is no primary liability on the part of lessee appellees to pay for

said loss. As recognized by this Court in the *American Surety Co.* case, supra, this distinction is determinative as to whether an insurer is entitled to be subrogated to the contract rights of the insured under a contract with a third person.

C. The subrogation clause contained in the policy issued by appellant to Dunwoody limited appellant's right of subrogation.

As heretofore set forth, appellant's claim in this action is based upon the principle that an insurer's right of subrogation arises by operation of law and is not dependent upon any express provision therefor in the policy (Br. 14). We have no quarrel with this principle. However, the question of the effect of a subrogation clause such as that contained in the policy issued by appellant to Dunwoody, on an insurer's equitable right of subrogation has not been raised in any of the cases cited by appellant in support of such claim (Br. 14-17).

That the equitable right of subrogation is not absolute, but may be limited by a provision in the policy[1], as was done in the instant case, was recognized by the Court in *Merchants Fire Assur. Corp. v. Hamil-*

[1]That the subrogation clause contained in the California Standard Form Fire Insurance Policy issued by appellant to Dunwoody limited the insurer's equitable right of subrogation was in effect recognized by the Legislature of the State of California when it changed the subrogation clause in the California Standard Form Fire Insurance Policy effective July 1, 1950. Said clause reads: "This company may require from the insured an asignment of all right of recovery against any party for loss to the extent that payment therefor is made by this company." (Section 2071 of the Fire Insurance Code of the State of California.)

ton Co. (1949, R.I.), 69 A. (2d) 551, wherein the subrogation clause construed by the Court was exactly the same as the subrogation clause contained in the policy issued by appellant to Dunwoody. In that case, the complainant issued to the respondent a fire insurance policy which contained a provision that if the complainant shall claim that the fire was caused by the act or neglect of any person or corporation the complainant shall, on payment of the loss, be subrogated to all right of recovery by the insured for the loss resulting therefrom and such right shall be assigned to the complainant by the assured on receiving such payment. Subsequently, the building insured was damaged by fire. The complainant paid the amount of loss to the respondent. Thereafter the complainant discovered that the fire was caused by the negligence of a third person and that the respondent had compromised an action which it had brought against said third person to recover from him the amount of loss or damage to the insured premises caused by the fire. In holding that the complainant was not entitled to be subrogated to the rights of the respondent against said third party in that it failed to comply with the provisions of the subrogation clause contained in the policy, the Court said at page 554:

> "This court has apparently recognized the general principle upon which the complainant chiefly relies which is in substance that an insurer's right of subrogation, a contract of fire insurance being one of indemnity, is not necessarily dependent upon the provisions of the policy alone

but exists as a recognized equitable right in the appropriate circumstances. * * *

"The recognition of the above broad principle of law does not, however, determine the instant cause. The respondent contends that such a right of subrogation as the complainant is here claiming, being personal in nature, may be modified, curtailed or defeated by a provision in the insurance contract entered into by the insured and the insurer. The respondent argues that the pertinent provision in the policy of insurance as set out in the bill of complaint, when properly construed, shows that the parties limited the complainant's right of subrogation by requiring as a condition to the maintaining of such a right that the complainant must, at or before the time of payment of the loss, assert its claim that the fire bringing about such loss was caused by the act or neglect of some third person.

"An examination of the cases called to our attention on the above point, in the judgment of a majority of the court, tends to show that the weight of such authority as there is supports the respondent's position that the provision in the insurance contract we have under consideration should be construed as requiring that the insurer make such a claim as above indicated and make it at or before the time it pays the loss if it desires later to enforce its right of subrogation.

"In Fire Association of Philadelphia v. Schellenger, 84 N.J.Eq. 464, 94 A. 615, 616, where the facts closely resembled those in the present cause and where the complainant was denied relief, a

provision in a fire policy in exactly the same language as the provision now before us was construed as follows: 'The rights of the parties to this litigation, therefore, must depend upon the meaning of the provision of the policy which deals with the matter of subrogation. It is plain from a reading of this part of the contract that the parties to it intended that the right of the insurer, in case it paid the loss, should not be an absolute, but a conditional one; the condition being that the insurer should "claim that the fire was caused by the act or neglect" of some third person.'

* * * * * * *

"Upon consideration it is the opinion of a majority of the court that the provision of the policy before us should be construed in accordance with the holdings in the cases relied on by the respondent, namely, to the effect that it is the intent and meaning of such provision that the right of the insurer to subrogation is not absolute but is on the condition that it make claim, at or before the time it pays the loss, that the fire was caused by the act or neglect of some third person. When issued the policy becomes the contract of the parties. It is reasonable to assume that the provision was inserted in the policy for some purpose. From its terms it does not appear to be a mere confirmatory restatement of the equitable principles governing subrogation generally, nor does it act to enlarge or increase them. On the contrary, when read as a whole its apparent object is to limit and place a condition upon the exercise of such right of subrogation." (Underscoring added.)

In the foregoing case the Court cited the following cases wherein the same construction and result were reached after consideration of the meaning of clauses identical with the one construed by it.

Firemen's Ins. Co. v. Georgia Power Co. (1935), 181 Ga. 621, 183 S.E. 799;

Home Ins. Co. v. Hartshorn (1922), 128 Miss. 282, 91 So. 1;

Fireman's Fund Ins. Co. v. Thomas (1934), 49 Ga. App. 731, 176 S.E. 690.

Appellant seeks to distinguish the *Merchants* case from the instant case in that the *Merchants* case was dealing with the right of subrogation to a tort liability whereas the instant case relates to a contract liability (Br. 16). Appellant ignores the fact that in the *Merchants* case, the Court determined that the equitable right of subrogation of an insurer may be enlarged or limited by a provision inserted in the policy and that when such provision is inserted in the policy then the subrogation rights of the insurer are to be determined solely by said provision. The Court drew no distinction between the equitable right of subrogation arising from contract liability and that arising from tort liability. That no such distinction is to be drawn is apparent from the fact that the subrogation clause construed by the Court in the *Merchants* case commences, as does the subrogation clause contained in the policy issued by appellant to Dunwoody, "If the company shall claim that the fire was caused by the act or neglect of any person * * *" and that the

Court construed said clause as requiring, as a condition to maintaining the right of subrogation, that the insurer must make such claim. In other words, the insurer's right of subrogation is limited to cases comprehended by the provisions of said clause, namely, to tort cases.

Appellant contends that in New Jersey and in Georgia, in which States the Courts have reached the same result as that reached by the Court in the *Merchants* case, the right of an insurer to subrogate against a third party whose liability is founded in contract has been upheld (Br. 17). In support of its contention appellant cites (Br. 17) *Leyden v. Lawrence* (N.J. 1911), 81 A. 121 and *Gainesville etc. Bank v. Martin* (Ga. 1939), 1 S.E. (2d) 636. In neither of these cases was an argument advanced that there was a subrogation clause in the policy which limited the insurer's equitable right of subrogation. It does not appear that the policies contained a subrogation clause the same or similar to that contained in the policy issued by appellant to Dunwoody.

Appellant cites *Field v. Western Etc. Ins. Co.* (N.Y. 1943), 48 N.E. (2d) 489, 146 A.L.R. 434, as a case wherein appellant contends the Court treated a policy of insurance as though it contained no subrogation clause at all because the subrogation clause contained in the policy was not applicable to the situation with which the Court was dealing (Br. 17). In that case, the Court merely held that a clause requiring the insured to assign all right of recovery against any party

for loss or damage did not give the insurer the right of subrogation to contract rights of the insured.

II.

APPELLANT'S ARGUMENT THAT THE LESSEE APPELLEES ARE NOT ENTITLED TO THE BENEFIT OF APPELLANT'S INSURANCE PAYMENT TO APPELLEE DUNWOODY IS IMMATERIAL TO THE ISSUE BEFORE THIS COURT.

Nowhere in the pleadings filed by the lessee appellees does it appear that they have taken the position, as contended by appellant (Br. 20), that the proceeds of appellant's policy inure to their benefit and are to be applied to the cost of restoration of the burned buildings. While it is true, as indicated by the answer of Dunwoody to Interrogatory No. 12 propounded to her by appellant (Br. 20), that appellees Harold F. Baruh and Harold A. Goldman have requested that Dunwoody apply the proceeds of her policy to the rebuilding of the destroyed buildings, no claim has been made by lessee appellees in this action that they are entitled to said proceeds. Whether they are or are not is immaterial to the aforesaid issue before this Court.

III.

SINCE THE TRIAL COURT RENDERED JUDGMENT IN FAVOR OF APPELLEES AND AGAINST APPELLANT, APPELLANT HAS NO RIGHT TO CLAIM IN THIS COURT RELIEF NOT PRAYED FOR IN ITS COMPLAINT.

In support of its contention that the trial Court "should have included in the judgment a declaration that upon full restoration of the buildings appellant would be entitled to a return of the amount so paid, and that in the event of a failure upon the part of lessees to fulfill their obligation to restore the buildings appellant would be entitled to be subrogated to appellee Dunwoody's right to enforce this obligation * * *" appellant cites Rule 54(c) of the Federal Rules of Civil Procedure which reads:

> "Demand for Judgment. A judgment by default shall not be different in kind from or exceed in amount that prayed for in the demand for judgment. Except as to a party against whom a judgment is entered by default, every final judgment shall grant the relief to which the party in whose favor it is rendered is entitled, even if the party has not demanded such relief in his pleadings." (Underscoring added.)

Appellant overlooks the fact that the trial Court rendered judgment in favor of the appellees in this action and against appellant. The foregoing rule only applies to judgments entered in favor of a party and therefore does not support appellant's contention.

IV.

CONCLUSION.

It is submitted that the trial Court's finding in favor of the lessee appellees on the issue before this Court is amply supported by the evidence and the law and therefore the judgment of the trial Court should be affirmed.

Dated, San Francisco, California,
October 1, 1951.

Respectfully submitted,
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Attorneys for Appellees Harold A. Goldman, Myrtle Goldman, Harold F. Baruh and Doris G. Baruh.

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